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In the Supreme Court of the United States

OCTOBER TERM, 1978

NATIONAL MUFFLERS DEALERS ASSOCIATION, INC.,
PETITIONER

v.

UNITED STATES OF AMERICA

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES

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OPINIONS BELOW

The findings of fact and conclusions of law of the district court (Pet. App. B, pp. 8a-15a) are not officially reported. The opinion of the court of appeals (Pet. App. A, pp. 1a-7a) is reported at 565 F.2d 845.

JURISDICTION

The judgment of the court of appeals (Pet. App. C, pp. 16a-17a) was entered on November 21, 1977.

The petition for a writ of certiorari was filed on February 18, 1978, and was granted on May 15, 1978 (A. 52a). The jurisdiction of this Court rests upon 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether an organization whose activities are directed solely toward the performance of services for the franchisees of a particular brand of a product, rather than the improvement of business conditions of those who deal in any brand of the product, is exempt from income tax as a "business league" under Section 501(c)(6) of the Internal Revenue Code of 1954 and the applicable Treasury Regulations.

STATUTE AND REGULATION INVOLVED

Section 501(a) and (c)(6) of the Internal Revenue Code of 1954 (26 U.S.C.), and Treasury Regulations on Income Tax, Section 1.501(c)(6)-1 (26 C.F.R.), are set forth in the Appendix, *infra*, pp. 36-38.

STATEMENT

1. Petitioner was organized in 1971 under the New York Not-For-Profit Corporation Law[1] as a trade association for muffler dealers franchised by Midas International Corporation. At that time, there was a contest for control of Midas, and many of Midas' franchisees organized petitioner in order to establish

[1] See New York Not-For-Profit Corporation Law § 402 (McKinney 1970) (A. 18a).

a united group to deal with the new Midas management (Pet. App. A, pp. 2a-3a; Pet. App. B, pp. 8a-10a).

Petitioner's articles of incorporation stated that it was formed "to foster and promote the interests of those individuals * * * engaged in business as muffler dealers * * * [and] to advance the trade and commerce of its members * * *" (A. 19a; Pltf. Ex. 8, A. 41a). However, petitioner's original by-laws adopted in April 1971 provided that only muffler dealers holding a valid Midas Muffler franchise were eligible for membership (A. 26a-27a). As part of its effort to obtain status as a tax-exempt business league, petitioner amended its by-laws on October 23, 1972, to permit "[a]ny muffler dealer holding a valid franchise as such [to] be eligible for membership" (A. 46a-47a).

Despite this amendment to its by-laws, petitioner has never broadened its membership to include non-Midas dealers. Throughout its history, petitioner has never had any member who is not a Midas Muffler franchisee. Moreover, petitioner has never attempted to solicit membership outside the Midas chain and recruit non-Midas dealers. A letter seeking new members sent by petitioner's president on November 27, 1975, contained the greeting "Dear Fellow Midas Dealer" (Pet. App. A, p. 3a; Pet. App. B, pp. 9a-10a). In that letter, petitioner's president, who was a Midas dealer himself, further stated: "In view of the fact that we are now working closely with Midas International officials in a joint endeavor to improve

the Midas program, I believe it is to the interest of every dealer that we have 100% representation. Now, for the first time, there is a genuine partnership between Midas, on the one hand, and the dealers, represented by our Association, on the other" (A. 49a-50a).

During 1971-1973, the years in question, approximately 290 (50 percent) of all Midas dealers were members of petitioner. As a result of petitioner's subsequent efforts, almost 80 percent of all Midas dealers had been enrolled by the end of 1975 (Pet. App. A, p. 3a; A. 18a, 49a). However, the bulk of the muffler industry continued to be excluded from petitioner's membership. This fact was confirmed by a survey undertaken at the request of petitioner and Midas that indicated that Midas dealers received only 21 percent of the replacement muffler business in 18 major metropolitan markets (Pet. App. A, p. 6a and n. 2).[2]

Since petitioner's organization, its principal activity has been to serve as a bargaining agent for its members in dealing with Midas. For example, petitioner negotiated a new franchise agreement, which petitioner's executive director characterized as

[2] Prior to trial, the district court denied both parties' motions for summary judgment on the ground that there was then as yet no evidence "regarding Midas International's share of the market or regarding what proportion of all muffler franchises belong to [petitioner]" (A. 24a). The court therefore concluded that "[a] factual determination would be necessary * * * [so that it] could determine whether or not [petitioner's] activities benefit the muffler industry as a whole (*ibid.*).

"almost a model franchise agreement." While the former franchise agreement could be canceled upon 30 days' notice, the new agreement had a 20-year term and could not be canceled except for cause. It also gave Midas dealers the right to sell the franchise, subject to Midas' approval of the buyer, and provided for succession in the event of the death of the dealer. Under the new agreement, disputes in these matters were made subject to arbitration (Pet. App. A, pp. 2a-3a; Pet. App. B, p. 10a; Tr. 21-25[2a]).

Petitioner also persuaded Midas to eliminate the practice that customers pay a service charge when seeking the otherwise free replacement of a guaranteed Midas muffler. Under the previous practice, Midas dealers applied the service charge against the cost of the replacement muffler; however, under the new agreement, Midas reimbursed the dealer for 95 percent of the cost and has eliminated the service charge. Petitioner also achieved a reduction in the prices that Midas charged the dealers for pipe, and obtained a commitment from Midas that its pipe prices would remain competitive. Petitioner thereafter monitored by computer the prices of Midas pipe and the competitors' prices, in order "to make sure that they are competitive and that they are kept low within the market" (Pet. App. A, p. 3a; Pet. App. B, pp. 10a-11a; Tr. 25-28).

Petitioner's activities also included the sponsorship of a group life and health insurance program, and a group casualty and workers' compensation program. These programs were available at reduced

[2a] "Tr." refers to the trial transcript.

cost to Midas dealers who are members. Petitioner also held an annual convention, at which issues of interest to Midas dealers are discussed, and sent periodic newsletters to its members (Pet. App. A, p. 3a; Pet. App. B, p. 10a; Tr. 29-30).

2. The Internal Revenue Service rejected petitioner's application for tax-exempt status as a "business league" under Section 501(c)(6) of the Code. After the Service denied its claims for refund of $5,357 in income taxes for the years 1971-1973, petitioner instituted this suit in the United States District Court for the Southern District of New York (Pet. App. B, pp. 8a-9a; A. 7a-12a).

The district court found that "there [was] no evidence that petitioner confers a benefit on the muffler industry as a whole or upon muffler franchisees as a group" (Pet. App. B, p. 11a). As the court observed, "[petitioner's] newsletter and other information are disseminated only to Midas dealers, and its bargaining activities, which constitute its most important function, are for the benefit of Midas dealers alone" (*ibid.*). The court also found that Midas dealers alone do not constitute a line of business because the applicable industry is the muffler industry and the applicable line of business is the business of muffler franchises taken as a whole. Since Treasury Regulations, Section 1.501(c)(6)-1 requires that a tax-exempt business league's activities be directed at the improvement of business conditions in "one or more lines of business," the district court held that petitioner was not entitled to tax exemption as a business league (Pet. App. B, pp. 11a-14a).

The court of appeals affirmed (Pet. App. A, pp. 1a-7a). It agreed with the district court that petitioner does not benefit an entire line of businesses as required by the Regulations, and therefore did not merit tax-exempt status. In the absence of an explicit statutory definition of "business league," the court of appeals examined the general characteristics of the organizations included with business leagues under Section 501(c)(6) exemption. In its view, the fact that the statute also exempted chambers of commerce and boards of trade showed that Congress intended to limit the Section 501(c)(6) exemption to those organizations that promote some aspect of the general economic welfare rather than some particular private interest.

In so ruling, the court explicitly refused to follow the contrary decision in *Pepsi-Cola Bottlers' Assn., Inc.* v. *United States*, 369 F.2d 250 (C.A. 7), which upheld the exempt status of an association composed solely of bottlers of a single brand of soft drink on the ground that the "line of business" requirement of the Regulation had no support in the statute (Pet. App. A, p. 5a n. 1). The court held that the requirement of the longstanding Treasury Regulation that a tax-exempt business league devote itself to the improvement of conditions in "one or more lines of business" reasonably implements the statute by insuring that the exemption benefits a sufficiently broad segment of the business community (Pet. App. A, pp. 4a-6a).

SUMMARY OF ARGUMENT

1. Section 501(c)(6) of the Internal Revenue Code of 1954 provides an income tax exemption for "[b]usiness leagues, chambers of commerce, real-estate boards, [and] boards of trade * * *." Although the Code does not define the term "business league," Treasury Regulations, Section 1.501(c)(6)-1, states in pertinent part as follows:

> A business league is an association of persons having some common business interest, the purpose of which is to promote such common interest and not to engage in a regular business of a kind ordinarily carried on for profit. It is an organization of the same general class as a chamber of commerce or board of trade. *Thus, its activities should be directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons.* * * * [Emphasis supplied.]

The legislative history of Section 501(c)(6), which was first enacted in 1913, confirms the correctness of the court of appeals' holding that "[t]he admittedly common characteristic of the organizations enumerated in § 501(c)(6) is that they foster well-being within a broadly-defined segment of the commercial sector" (Pet. App. A, p. 5a). The submissions to Congress for exemption were on behalf of chambers of commerce and boards of trade and the legislative evidence supports limiting the Section 501(c)(6) exemption to those organizations that resemble chambers of commerce or boards of trade. Thus, a tax-exempt business league must benefit a broad spectrum of the business of a geographic area or a particular industry.

The decision below therefore properly concluded that in enacting Section 501(c)(6), Congress intended "to provide an exemption for organizations which promote some aspect of the general economic welfare rather than support particular private interests" (*ibid.*). As the court of appeals observed, the "'line of business'" requirement of the Regulations is "well suited to assuring that an organization's efforts do indeed benefit a sufficiently broad segment of the business community" (*ibid.*; footnote omitted). Indeed, the "line of business" requirement has been in the Regulations since 1929 and has stood without change through many successive reenactments of the statute. The decisions of this Court have long held that such a Treasury Regulation is entitled to great weight in construing the statute and must be sustained unless unreasonable and plainly inconsistent with the statute. See, *e.g.*, *Bingler* v. *Johnson*, 394 U.S. 741, 749-750; *Helvering* v. *Winmill*, 305 U.S. 79; *Lykes* v. *United States*, 343 U.S. 118.

2. Petitioner does not challenge the validity of the Regulation or the court of appeals' conclusion that it does not meet the "line of business" requirement of the Regulation. Unlike a chamber of commerce or a board of trade that draws its membership from one or more lines of business, petitioner's members are all franchisees of Midas International Corporation

engaged in the sale and service of Midas Mufflers. Moreover, petitioner's activities do not benefit the muffler industry as a whole but are solely directed toward serving the interests of Midas International and the Midas dealers in their relationship with their franchisor. The court of appeals therefore correctly held that petitioner was not entitled to tax-exempt status under Section 501(c)(6) and the "line of business" requirement of the Regulation.

In urging that it is entitled to exemption as a business league, petitioner argues that the "line of business" requirement of the Regulation is merely illustrative of the overriding provision in the first sentence that the organization promote the common business interest of its members. But the courts have consistently held that the "line of business" requirement is one of several independent conditions each of which must be met in order to qualify for exempt status. Petitioner's construction would effectively read the line of business requirement out of the Regulation.

3. The court of appeals correctly declined to follow the contrary decision in *Pepsi-Cola Bottlers' Assn., Inc.* v. *United States*, 369 F.2d 250 (C.A. 7). There, a divided panel held that an organization of bottlers of a particular soft drink qualified as a tax-exempt business league despite the fact that its activities were solely directed toward promoting the interests of Pepsi-Cola and its bottlers rather than the soft drink industry as a whole.

The legislative history of Section 501(c)(6) demonstrates that Congress intended to limit the business league exemption to those organizations that are similar to chambers of commerce and boards of trade. An organization such as petitioner or the Pepsi-Cola Bottlers' Association formed for the purpose of promoting the business of a single manufacturer and its distributors is unlike a chamber of commerce or a board of trade because its activities are not directed to the improvement of business conditions of one or more lines of business. As the dissenting judge in the *Pepsi-Cola* case observed in terms equally appropriate to petitioner's claim: "Bottling Pepsi-Cola is not a line of business. It is only one of a line—one of many competing businesses in the cola and soft drink industry" (*id.* at 253). The Seventh Circuit therefore erred in permitting the Pepsi-Cola Company to obtain a tax exemption for an organization devoted principally to improving its market position against its competitors in the soft drink industry.

ARGUMENT

PETITIONER DOES NOT QUALIFY AS A TAX-EXEMPT BUSINESS LEAGUE UNDER SECTION 501(c)(6) AND THE APPLICABLE REGULATIONS BECAUSE ITS ACTIVITIES ARE DIRECTED SOLELY TOWARD THE PERFORMANCE OF SERVICES FOR THE DEALERS OF A PARTICULAR BRAND OF A PRODUCT RATHER THAN THE IMPROVEMENT OF BUSINESS CONDITIONS OF THOSE WHO DEAL IN ANY BRAND OF THE PRODUCT

The question presented in this federal income tax case involves the scope of the exemption for "business leagues" provided by Section 501(c)(6) of the Internal Revenue Code of 1954, Appendix, *infra*, p. 36. Section 501(a) of the Code accords exempt status to "[a]n organization described in subsection (c) * * *," which in turn sets forth a list of tax-exempt organizations. Subparagraph (6) defines one such category of exempt organization as "[b]usiness leagues, chambers of commerce, real-estate boards, boards of trade, or professional football leagues (whether or not administering a pension fund for football players), not organized for profit and no part of which inures to the benefit of any private shareholder or individual." The exemption for business leagues, chambers of commerce, and boards of trade has its genesis at the inception of the modern income tax in 1913.[3]

[3] See Income Tax Act of 1913, Section II, G.(a), 38 Stat. 172. See also S. Rep. No. 80, 63d Cong., 1st Sess., pp. 25-26 (1913), which states in pertinent part:

> Paragraph F is amended so as to provide that nothing in this section of the bill shall apply to "business leagues, nor to chambers of commerce or boards of trade, not organized for profit of a private stockholder or individual; nor to any civil league or organization not organized for profit, but operated exclusively for the promotion of social welfare."

See also H.R. Conf. Rep. No. 86, 63d Cong., 1st Sess., p. 26 (1913); "Tariff Schedules," *Briefs and Statements* filed with the Senate Committee on Finance on H.R. 3321, 63d Cong., 1st Sess., Vol. III, pp. 2001-2003, 2040 (1913) (reprinted in "Tariff Schedules, Free List," *Briefs and Statements* filed with the Senate Committee on Finance on H.R. 3321, 63d Cong., 1st Sess., pp. 1987-1989, 2006 (second print 1913)).

The exemption for real estate boards was added in 1928. See Section 103(7), Revenue Act of 1928, 45 Stat. 813. See H.R. Rep. No. 2, 70th Cong., 1st Sess., p. 17 (1927); S. Rep. No. 960, 70th Cong., 1st Sess., p. 25 (1928); Hearings on Revenue Revision, 1927-1928, before the House Committee on Ways and Means, interim 69th-70th Congs., pp. 235-239, 261, 268, and 269 (1927); Hearings on H.R. 1, the Revenue Act of 1928, before the Senate Committee on Finance, 70th Cong., 1st Sess., pp. 169, 176 (1928).

The exemption for football leagues was added by the Act of November 8, 1966, Section 6(a), 80 Stat. 1515. See H.R. Conf. Rep. No. 2308, 89th Cong., 2d Sess., pp. 9-10 (1966); Summary of the Act Temporarily Suspending the Investment Credit, etc., Joint Committee on Internal Revenue Taxation, 89th Cong., 2d Sess., p. 22 (1966); 112 Cong. Rec. 26886-26887 (1966); 112 Cong. Rec. 28226, 28228 (1966).

Although the Code does not define "business league," the Regulations have long marked out the contours of the statutory term. Treasury Regulations, Section 1.501(c)(6)-1 provides in pertinent part as follows:

> A business league is an association of persons having some common business interest, the purpose of which is to promote such common interest

and not to engage in a regular business of a kind ordinarily carried on for profit. It is an organization of the same general class as a chamber of commerce or board of trade. *Thus, its activities should be directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons.* * * * [Emphasis added.]

This definition was first promulgated in 1929 in Treasury Regulations 74, Art. 528 (1928 Revenue Act), and has stood without change for almost half of a century through all succeeding revenue acts.[4] During this period, four circuits and the Court of Claims have upheld this regulatory definition of "business league" as a valid interpretation of the statute. See, *e.g.*, *Indiana Retail Hardware Assn.* v. *United States*, 366 F.2d 998, 999 (Ct. Cl.); *Evanston-North Shore Board of Realtors* v. *United States*, 320 F.2d 375 (Ct. Cl.), certiorari denied, 376 U.S. 931;

[4] See Treasury Regulations 77, Art. 528 (1932 Revenue Act); Treasury Regulations 86, Art. 101(7)-1 (1934 Revenue Act); Treasury Regulations 94, Art. 101(7)-1 (1936 Revenue Act); Treasury Regulations 101, Art. 101(7)-1 (1938 Revenue Act); Treasury Regulations 103, Sec. 19.101(7)-1 (1939 Code); Treasury Regulations 111, Sec. 29.101(7)-1 (1939 Code); Treasury Regulations 118, Sec. 39.101(7)-1 (1939 Code).

The earlier regulations are as follows: Treasury Regulations 33, Art. 87 (1913 Revenue Act); Treasury Regulations 45, Art. 518 (1918 Revenue Act); Treasury Regulations 62, Art. 518 (1921 Revenue Act); Treasury Regulations 65, Art. 518 (1924 Revenue Act); Treasury Regulations 69, Art. 518 (1926 Revenue Act).

United States v. *Oklahoma City Retailers Assn.*, 331 F.2d 328 (C.A. 10); *Automotive Electric Assn.* v. *Commissioner*, 168 F.2d 366 (C.A. 6); *Apartment Operations Assn.* v. *Commissioner*, 136 F.2d 435 (C.A. 9); *Underwriters' Laboratories* v. *Commissioner*, 135 F.2d 371 (C.A. 7), certiorari denied, 320 U.S. 756.

We submit that the decision below correctly held that petitioner does not qualify as a tax-exempt "business league" under Section 501(c)(6) and the applicable Regulations. Petitioner is not "an organization of the same general class as a chamber of commerce or board of trade" whose "activities * * * [are] directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons" (Treasury Regulations, Section 1.501(c)(6)-1). To the contrary, petitioner's activities are solely for the benefit of its limited constituency of Midas Muffler dealers to the exclusion of the rest of the muffler industry. As we shall demonstrate, the legislative history of Section 501(c)(6) and the case law confirm that petitioner's primary purpose—improving business conditions for Midas dealers—is an insufficient basis for exemption as a "business league."

A. The legislative history confirms the reasonableness of the regulation's requirement that a tax-exempt business league's activities must be directed to the improvement of business conditions of one or more lines of business.

1. As originally enacted in 1913, the predecessor of Section 501(c)(6) conferred an income tax exemption upon "business leagues" "chambers of commerce," and "boards of trade." While the committee reports do not define these terms, the legislative history indicates that Congress intended to limit the scope of the exemption to those organizations that benefit a broad sector of the business community. Thus, during the Senate Finance Committee hearings that preceded the enactment of the statute, the General Secretary of the United States Chamber of Commerce emphasized the public purpose and civic role of such organizations as follows: [5]

> While * * * [the commercial organization's] original reason for being is commercial advancement, it is not in the narrow sense of advantage to the individual, but in the broad sense of building up the trade and commerce of the community as a whole and with the fullest recognition of the facts that business can not permanently prosper at the expense of other classes, and that what is expended in improving the city in which

[5] "Tariff Schedules," *Briefs and Statements* filed with the Senate Committee on Finance on H.R. 3321, 63d Cong., 1st Sess., Vol. III, pp. 2001-2003 (1913) (reprinted in "Tariff Schedules, Free List," *Briefs and Statements* filed with the Senate Committee on Finance on H.R. 3321, 63d Cong., 1st Sess., pp. 1987-1989 (second print 1913)).

> it is situated and the conditions of its inhabitants will inevitably redound to the benefit of its commercial interests.

A subsequent statement submitted to the Senate Finance Committee by the Chamber of Commerce urged exemption of "chambers of commerce and similar organizations" because such organizations benefit "all other members * * * of their industries" and increase incomes "not of themselves, but * * * irrespective of membership in the organizations" "Tariff Schedules," *Briefs and Statements, supra*, note 3, p. 13 at pp. 2002, 2003 (second print, pp. 1988-1989).[6]

Similarly, in 1928, when Congress added "real estate boards" to the exemption covering business leagues, it took note of the fact that the 687 real estate boards were "among the livest [sic] cooperating nonprofit enterprises in this country," and "* * * [were] organized for the purpose of the promotion and facilitating of business, like a business league

[6] At the time of the enactment of the original statute, the American Warehousemen's Association submitted the following statement (see "Tariff Schedules," *Briefs and Statements, supra*, at 2040 (second print, p. 2026)):

> Exemption is asked only for commercial organizations which are not organized for profit. These organizations receive their income from dues paid by their members, a form of voluntary tax which business men pay that they may receive *in common with all other members of their communities or of their industries* the benefits of cooperative study of local development, of civic affairs, of industrial resources, and of local, national, and international trade. In fine, these organizations are cooperative agencies of good citizenship in industry and commerce. [Emphasis added.]

or chamber of commerce * * *" by providing information as to the character, utility, and value of real property within a particular geographic area. See House Hearings, Revenue Revision, 1927-1928, *supra*, at pp. 236, 237 (Statement of Nathan William MacChesney). Since Congress "never intended that real estate boards should be taxed," it "had no objection to * * * saying so." House Hearings, *supra*, at 238 (statement of Rep. Chindblom). The pertinent House Committee report therefore concluded that real estate boards were "within the purpose of the section" (H.R. Rep. No. 2, 70th Cong., 1st Sess. 17 (1927)).

Two points emerge with clarity from the foregoing legislative history. First, Congress used the terms "business leagues," "chambers of commerce," and "boards of trade" to indicate organizations of the same general class. This is demonstrated by the 1929 addition of "real estate boards" as conforming to the original congressional purpose in enacting the statutory exemption for chambers of commerce and boards of trade. Thus, in order for an organization to qualify for tax exemption as a business league, it must be of the same character as a chamber of commerce or a board of trade. For a chamber of commerce, the pertinent sector is all business located within a particular geographic area. A board of trade likewise relates to a geographic area but may be limited to only one or more lines of business.[7]

[7] See *Retailers Credit Assn.* v. *Commissioner*, 90 F.2d 47, 51 (C.A. 9). In considering whether an organization was an exempt business league, the court adopted the following definitions of chamber of commerce and board of trade:

> A chamber of commerce is defined by Webster's New International Dictionary to be "A board or association to promote the commercial interest of a locality, a country, or the like." In 11 C.J. 228, and Bouv. Law Dict. (Rawle's 3rd Rev.), it is defined as "a society of a city, who meet to promote the general trade and commerce of the place." * * *
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> * * * *
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> A board of trade is defined in Webster's New International Dictionary as "a body of men organized for the advancement and protection of business interests." Although the terms "chamber of commerce" and "board of trade" are nearly synonymous, there is a slight distinction between their meanings. The former relates to all businesses in a particular geographic location, while the latter may relate to only one or more lines of business in a particular geographic location, but need not relate to all.

See also Rev. Rul. 73-411, 1973-2 Cum. Bull. 180; L.O. 1121, III-1 Cum. Bull. 275, 279-280 (1924).

Second, in order for an organization to resemble a chamber of commerce or a board of trade for purposes of the exemption, it must benefit a broad sector of the business community. The statements of the United States Chamber of Commerce prior to the enactment of the original statute in 1913 and on behalf of the National Association of Real Estate Boards in 1927 in support of the exemption for real estate boards emphasize the semi-public and civic nature of their organizations, their activities in building the trade and commerce of the community, and the resulting benefits to both members and nonmembers alike.

2. The administrative and judicial precedents similarly reflect the congressional purpose to limit the business league exemption to those organizations that resemble chambers of commerce or boards of trade by benefiting a broad segment of the business community. In 1924, the then Bureau of Internal Revenue issued a law opinion concluding that a stock exchange was not an exempt business league. In so ruling, the Bureau stated as follows (L.O. 1121, III-1 Cum. Bull. 275, 280-281 (1924)):[8]

> Under the well-established maxim *noscitur a sociis*, the meaning of a word used in a statute must be construed in connection with the words with which it is associated. Although it is undoubtedly true, as stated in article 518 of Regulations 62, that a business league does not need to be similar in all respects to a chamber of commerce or board of trade, nevertheless it appears under the accepted principles of statutory construction that Congress must have used the expressions "business leagues," "chambers of commerce," and "boards of trade" to indicate organizations of the same general class, having for their primary purpose the promotion of business welfare. Although it may be true that stock exchanges incidentally contribute to the promotion of business welfare and indirectly contribute to business prosperity, nevertheless their primary purpose is to afford facilities to a limited class of people for the transaction of their private business. Therefore, stock exchanges are not business leagues, chambers of commerce, or boards of trade within the meaning of section 231.

[8] Pursuant to the program announced in Rev. Proc. 67-6, 1967-1 Cum. Bull. 576, for the review of rulings issued prior to 1953, L.O. 1121, *supra*, was declared obsolete by Rev. Rul. 68-207, 1968-1 Cum. Bull. 577, 578. However, the reasoning and result of L.O. 1121 continues to represent the governing law applicable to the business league exemption. It was declared obsolete because the Regulation since 1925 has expressly denied exempt status to stock exchanges. T.D. 3746, IV-2 Cum. Bull. 77 (1925). See Treasury Regulations, Section 1.501(c)(6)-1, Appendix, *infra*, pp. 37-38, which provides "A stock or commodity exchange is not a business league, a chamber of commerce, or a board of trade within the meaning of Section 501(c)(6) and is not exempt from tax."

Three years later, the Board of Tax Appeals ruled that a corporation organized by associations of insurance companies to provide printing services for their member companies was not an exempt business league. *Uniform Printing & Supply Co.* v. *Commissioner*, 9 B.T.A. 251, affirmed, 33 F.2d 445 (C.A. 7), certiorari denied, 280 U.S. 591. In so holding, the Board reaffirmed the Treasury's position, based upon the legislative history, that "a business league, to be entitled to the exemption, should be engaged in and limited to activities similar to those of the ordinary chamber of commerce or board of trade * * *" (9 B.T.A. at 254). As a result of that decision, the Commissioner revised the Regulation to its present form in 1929 in order to incorporate the rule that the business league exemption is limited to organiza-

tions of the same general class as a chamber of commerce or board of trade.[9]

Since the principal characteristic of a chamber of commerce or a board of trade (and the characteristic that motivated the tax exemption) is that it benefits a broad spectrum of the business community, the rule that a tax-exempt business league resemble a chamber of commerce or board of trade includes the corollary requirement that it direct its activities toward improving conditions in at least one line of business.

The correctness of this proposition was early recognized by the courts. Thus, in *Produce Exchange Stock Clearing Ass'n* v. *Helvering*, 71 F.2d 142 (C.A. 2), the court denied an exemption to a stock clearing association that performed services only for its own members and not for the line of business encompassing all brokers trading on the New York Produce Exchange. In terms equally appropriate to petitioner's claim in this case, the court stated (*id.* at 143-144):

> The petitioner's activities are solely for the direct benefit of its so-called "clearing members." Nothing is done to advance the interests of the community or to improve the standards or conditions of a particular trade, as in the case of chambers of commerce, real estate boards, and boards of trade. Under the familiar doctrine of noscitur a sociis, a business league to be exempt must possess the general characteristics of these

[9] See and compare Treasury Regulations 69, Art. 518 (1926 Revenue Act) with Treasury Regulations 74, Art. 528 (1928 Revenue Act).

> other organizations with which the statute groups it.

Accord; *Evanston-North Shore Board of Realtors* v. *United States*, 320 F.2d 375, 379-380 (Ct. Cl.) (Reed, J.), certiorari denied, 376 U.S. 931; *Automotive Electric Assn.* v. *Commissioner*, 168 F.2d 366, 367-368 (C.A. 6); *Park West-Riverside Associates, Inc.* v. *Commissioner*, P-H B.T.A. Memo., par. 39,251, affirmed *per curiam*, 110 F.2d 1022 (C.A. 2); *Retailers Credit Assn.* v. *Commissioner*, 90 F.2d 47, 50 (C.A. 9); *American Fisherman's Tuna Boat Ass'n* v. *Rogan*, 51 F. Supp. 933, 936 (S.D. Cal.); *Northwestern Municipal Ass'n* v. *United States*, 22 F. Supp. 18, 22 (D. Minn.).

3. The foregoing legislative history and case law confirm the correctness as well as reasonableness of the Regulation's requirement that the activities of a tax-exempt business league "should be directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons." As this Court has consistently held, "[I]t is fundamental * * * that as 'contemporaneous constructions by those charged with administration of' the Code, [Treasury] Regulations 'must be sustained unless unreasonable and plainly inconsistent with the revenue statutes' and 'should not be overruled except for weighty reasons.'" *Bingler* v. *Johnson*, 394 U.S. 741, 749-750, quoting from *Commissioner* v. *South Texas Lumber Co.*, 333 U.S. 496, 501. Accord: *Fulman* v. *United States*, 434 U.S. 528, 532-533; *United States*

v. *Correll*, 389 U.S. 299, 306-307; *Better Business Bureau* v. *United States*, 326 U.S. 279, 286. This rule of deference is particularly appropriate here because the Regulation constitutes a long-standing administrative interpretation for almost 50 years and has been in effect during successive reenactments of the statute that have included extensive revision of the exempt organization provisions. *Helvering* v. *Winmill*, 305 U.S. 79, 83; *Lykes* v. *United States*, 343 U.S. 118.[10]

Here, as we have pointed out (*supra*, pp. 16-22), the line of business requirement of the Regulations implements the congressional purpose of limiting the business league exemption to those organizations that possess the same general characteristics as chambers of commerce and boards of trade. For a chamber of commerce, the pertinent sector is a geographic area; for a board of trade, a particular business or industry is the focus of attention so that its membership would be composed of competing businesses. The purpose of Section 501(c)(6) is therefore to provide an exemption for organizations that promote some aspect of the general economic welfare rather than support particular private interests.

An organization confined to the distribution chain of a single brand or manufacturer does not promote the general economic welfare in the manner of a chamber of commerce or a board of trade. To the contrary, such an organization is much more likely to

[10] Compare Section II, G.(a) of the Income Tax Act of 1913 with the 21 paragraphs devoted to exempt organizations in the current version of Section 501(c) of the 1954 Code.

perform particular services for individual persons rather than to seek the improvement of business conditions for a broad segment of the business community. Thus, the line of business requirement effectively distinguishes between those organizations that advance particular narrow private interests and those that are involved in promoting the commercial activity of the community as a whole or a specific industry. As the court of appeals correctly concluded, "[t]he 'line of business' requirement contained in the regulations is well suited to assuring that an organization's efforts do indeed benefit a sufficiently broad segment of the business community" (Pet. App. A, p. 5a; footnote omitted).

B. Petitioner does not meet the line of business requirement of the regulations because its activities only serve the interests of Midas Muffler Dealers and do not benefit the muffler industry as a whole.

1. Given the reasonableness of the line of business requirement of the Regulations and applying it to the facts of this case, it is readily apparent that petitioner's activities are not "directed to the improvement of business conditions of one or more lines of business." It therefore does not merit exemption as a business league.

As the court of appeals observed (Pet. App. A, p. 6a), petitioner does not draw its franchise members from the broad base of muffler dealers generally but limits its rolls to Midas Muffler dealers. Despite the technical eligibility of "[a]ny muffler dealer holding a valid franchise" (A. 47a), it is undisputed that all

of petitioner's members are franchisees of a single manufacturer—Midas International Corporation. Indeed, petitioner's activities of serving the exclusive interests of Midas dealers in their day-to-day relations with their franchisor reflect its limited constituency. Thus, for example, petitioner negotiated a better contract and obtained price reductions solely for Midas dealers, published a news letter and held conventions for Midas dealers, and provided a group insurance program for its member Midas dealers. In its solicitation for new members, petitioner announced a program to establish committees "at Midas' suggestion—to help make the Midas program an ongoing source of profit for everyone" (Ex. D, A. 50a). On these facts, petitioner can hardly quarrel with the district court's finding approved by the court of appeals that "it failed to establish that it conferred any benefit on muffler dealers in general" (Pet. App. A, pp. 6a-7a; Pet. App. B, p. 11a).

2. a. Petitioner does not directly challenge the validity of the line of business requirement of the Regulation. Instead, it argues (Br. 25) that the paramount criterion for qualification as an exempt business league is set forth in the first sentence of the Regulation, *i.e.*, that the organization be "an association of persons having some common business interest, the purpose of which is to promote such common interest and not to engage in a regular business of a kind ordinarily carried on for profit." Petitioner (Br. 25) dismisses as merely "illustrative" of the "common business requirement" the second and third sentences of the Regulation that equate a business league to a chamber of commerce or a board of trade and provide that its activities be directed to the improvement of business conditions of one or more lines of business.

But the plain language of the Regulation refutes petitioner's attempt to brush aside the line of business requirement as an illustration of qualification under the common business interest test. The portions of the Regulation setting forth the analogy to chambers of commerce and the line of business requirement are not prefaced with the phrase "for example" or any other qualifying term that would suggest they are merely illustrative. To the contrary, they have substantive force as separate and independent tests to qualify for exempt status. Indeed, petitioner's variant reading of the Regulations has been flatly rejected by a uniform body of case law holding that to be qualified for exemption under Section 501(c)(6) an organization must meet *each* of the following conditions: (1) it must be a business league; (2) it must not be organized for profit; (3) it must be an organization no part of the net earnings of which inures to the benefit of any private shareholder or individual; (4) it must be an association of persons, incorporated or unincorporated, having common business interests the purpose of which is to promote those common interests; (5) its activities must be directed at improving the business conditions of one or more lines of business and not particular services for individual persons, and (6) it

may not engage in a business ordinarily carried on for profit. If any of these conditions is not met, the exemption is not applicable.[11] *United States* v. *Oklahoma City Retailers Assn.*, 331 F.2d 328, 331 (C.A. 10); *Indiana Retail Hardware Assn.* v. *United States*, *supra*, 366 F.2d at 1000; *Evanston-North Shore Board of Realtors* v. *United States*, *supra*, 320 F.2d at 377.[12]

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[11] Even on the assumption that petitioner's interpretation of the Regulation is correct, its exclusion of competing non-Midas dealers disqualifies it under the "common business interest" test that it urges is the paramount criterion for exemption. As a leading commentator on trade associations has observed, the common business interest presumes an association of competing businesses. See Webster, *The Law of Associations* 223 (1971):

> The meaning and import of the first requirement [common business interest] are certain. In all of the administratively and judicially approved associations the organization involved was composed of professionals or businessmen or business representatives in a competitive relationship with one another, sharing a common denominator of interest, who joined together to improve business or professional conditions generally while still maintaining the competitive relationship.

[12] The *amicus* Pepsi-Cola Bottlers Association similarly argues (Br. 26-27) that the Regulation's disqualification of organizations engaged in profit-making businesses or in the performance of particular services for members is sufficient to limit the exemption to organizations that serve the common business interests of its members. In the *amicus*' view (Br. 13), "[t]he distinction drawn by the relevant language of the Regulation is not between broad and narrow industry groups but between activity directed to the common interest of the

membership in improving the conditions which underlie their respective businesses and activity directed to generating particular profits or economies for individual members." The *amicus* reads the phrase "as distinguished from" that separates the line of business requirement from the prohibition against the performance of particular services as suggesting that any organization that refrains from performing services for individuals meets the common business test and is therefore exempt (see Br. 22).

But this argument ignores the independent positive command of the Regulation that the organization's activities "be directed to the improvement of business conditions of one or more lines of business." Instead, it focuses solely on the negative portion of the sentence that the organization should not engage in "the performance of particular services for individual persons" and equates that aspect of the Regulation with the common business interest requirement. In order to qualify for exemption, an organization must meet both the positive line of business requirement and avoid the activities that the Regulation deems inconsistent with exempt status. Thus, the fact that an organization does not engage in the performance of particular services for individual persons is not a sufficient basis for exemption.

Accordingly, the plain language of the Regulation refutes the *amicus*' reading that would elevate one condition for qualification at the expense of another. As the courts have uniformly held (see *supra*, pp. 27-28), qualification requires meeting each condition of the Regulation. *Washington State Apples, Inc.* v. *Commissioner*, 46 B.T.A. 64, *acq.* 1942-1 Cum. Bull. 17, upon which the *amicus* relies (Br. 12-14, 19, 24, 30), is not to the contrary. There, the Board recognized and applied the requirement that a tax-exempt business league's activities be directed to the improvement of one or more lines of business (46 B.T.A. at 69). The pertinent line of business was apple growing and shipping in the State of Washington and any person engaged in that activity was eligible for membership in the taxpayer (*id.* at 66). In holding that the taxpayer was engaged in improving the general commercial welfare of the community as a whole because of the importance of the apple industry in Washington, the Board noted that the taxpayer's

b. Petitioner further argues (Br. 4) that it is entitled to an exemption as a trade association of muffler dealers. To be sure, a trade association that meets the various conditions of the Regulation are typical exempt business leagues under Section 501(c)(6). See generally Webster, *supra*, at 223. But it defies common understanding to assert that a trade association can consist entirely of distributors or promoters of one brand, to the exclusion of competitors. To the contrary, an association designed to facilitate promotion or distribution of a particular brand of product, to the exclusion of all dealers handling competing brands, is not a trade association within the accepted meaning of that term. The standard definitions of a trade association invariably state that it includes business competitors in a given industry. For example, the Department of Commerce defines a trade association as a "nonprofit, cooperative, voluntarily-joined, organization of business competitors, designed to assist its members and its industry in dealing with mutual problems in several of

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advertising did not mention any brand name or particular grower but only the varieties of apples grown in Washington (*id.* at 69). Accord: *American Fishermen's Tuna Boat Ass'n* v. *Rogan*, 51 F. Supp. 933 (S.D. Cal.).

Rev. Rul. 67-252, 1967-1 Cum. Bull. 195, upon which the *amicus* also relies (Br. 17-18, 22, 30), is similarly distinguishable. There, the Service ruled that a non-profit corporation formed by processors, packagers, and distributors of a processed agricultural product to promote the sale of that product was exempt under Section 501(c)(6). But unlike this case, there is no suggestion that the activities of the organization were limited to promoting a particular brand.

the following areas: accounting practices, business ethics, commercial and industrial research, standardization, statistics, trade promotion, and relations with government, employees, and the general public."[13] Likewise, since 1929, the Federal Trade Commission has defined a trade association as a "nonprofit organization * * * of business competitors for the promotion of one or more economic interests of those in the line of business, or of the members, in the territory covered."[14] Indeed, a genuine trade association of competitors would not have paid, as did petitioner, 50 percent of the cost of a market study in order to "maintain and strengthen" the position of Midas in the muffler replacement business (Tr. 94, 97, 107; Ex. E, p. i). Nor would it have accepted Midas' suggestion to establish committees "to help make the Midas program an ongoing source of profit for everyone" (A. 50a). In short, petitioner's acknowledged

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[13] Judkins, *National Associations of the United States*, U.S. Dept. of Commerce, p. viii (1949), accord, *National Trade & Professional Associations of the United States and Canada* p. 5 (1978). In 1941, a government study similarly defined a trade association as a 'voluntary, nonprofit organization of enterprises engaged in a particular kind of business. Such enterprises may be individuals, partnerships, or corporations, and in nearly all associations are competitors." *Investigation of Concentration of Economic Power*, Temporary National Economic Committee, Monograph No. 18, Trade Association Survey, p. 1, 76th Cong., 3d Sess. (Senate Committee Print 1941).

[14] *Open-Price Trade Associations*, S. Doc. No. 226, 70th Cong., 2d Sess. i (1929). This report was published in the same year that the predecessor of Treasury Regulations, Section 1.501(c)(6)-1 was amended to include the line-of-business requirement.

exclusion of competing non-Midas dealers and its activities in promoting the products of Midas flatly contradict its claim that it is a trade association of muffler dealers.[15]

c. Finally, petitioner argues that it is entitled to a business league exemption because it has created an "economic balance" that would otherwise be lacking as a result of "the inherently unequal economic power between the individual franchisee and the monolithic franchisor" (Br. 20). In petitioner's view, "[t]his balancing of economic power is clearly in furtherance of the economic public policy of the United States and was intended by Congress to be encouraged" (Br. 9-10).

However admirable petitioner's goals and accomplishments on behalf of the Midas dealers may be, they bear no relationship to the criteria for qualification under Section 501(c)(6) and the applicable Regulation. As the court of appeals properly observed in rejecting this claim, "Whatever its merits, that argument is more appropriately directed to Congress. Nothing in the statute empowers the courts to grant tax exemptions to organizations, however novel, which

[15] Petitioner also suggests (Br. 24-25) that a nationwide franchisee organization is equivalent to a football league, which Congress added to the Section 501(c)(6) list of exempt organizations in 1966. But nothing in the legislative history of the 1966 amendment would support such a novel reading of the statutory exemption for "professional football leagues (whether or not administering a pension fund for football players)."

serve merely some public interest but not the broad interest intended by Congress" (Pet. App. A, p. 7a).[16]

3. The sole authority supporting petitioner's claim to tax-exempt status as a business league is *Pepsi-Cola Bottlers' Assn., Inc.* v. *United States*, 369 F.2d 250 (C.A. 7). There, a divided panel held that an organization of Pepsi-Cola Bottlers formed to "extend, further, protect, and improve the trade and business of bottling and selling Pepsi-Cola" (*id.* at 251) rather than the soft drink industry as a whole met the line of business requirement of the Regulation and qualified as a tax-exempt business league. The majority accordingly concluded that "[t]he plaintiff Association cannot be disqualified merely because its members all bottle a particular soft drink product. It is unreasonable to write into the statute a limitation wholly unsupported by the legislative history" (*id.* at 252).

But as we have pointed out *supra*, pp. 16-22, the legislative history demonstrates that Congress intended to limit the business league exemption to those

[16] Petitioner relies (Br. 15-18) on two rulings issued by the Internal Revenue Service according exempt status to employer associations that bargain collectively with employees and labor groups. (Rev. Rul. 65-164, 1965-1 Cum. Bull. 238), and to industry associations that promote legislation relating to common industry problems (Rev. Rul. 61-177, 1961-2 Cum. Bull. 117). But contrary to petitioner's argument, these rulings were not issued on the ground that the organizations performed activities that advance public policy. Rather, the rationale of the rulings was that the organizations represented businesses on an industry-wide basis and thereby met the line of business requirement of the Regulation.

organizations that are similar to chambers of commerce and boards of trade. An organization financed by the Pepsi-Cola Company for the purpose of increasing the sales of Pepsi-Cola whose membership is limited to bottlers of Pepsi Cola (*id.* at 251) is not analogous to a chamber of commerce or a board of trade. Like petitioner, its activities are limited to promoting the business of a single manufacturer and not to the improvement of business conditions of one or more lines of business. The Seventh Circuit therefore erred in permitting the Pepsi-Cola Company to obtain a tax exemption for an organization devoted solely to improving its market position against its competitors in the soft drink industry. See Note, *Taxation—Business League Exemption*, 35 Fordham L. Rev. 738 (1967).[17] As the dissenting judge observed in terms equally appropriate to this case (369 F.2d 253):

> Bottling Pepsi-Cola is not a line of business. It is only one of a line—one of many competing businesses in the cola and soft drink industry. And the services rendered by the Association to its members are not incidental to a general purpose of improving business conditions. They are essential to an express general purpose, the improvement of the members' competitive position as against nonmembers.

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[17] Shortly after the *Pepsi-Cola* decision, the Internal Revenue Service announced that it would not follow it. See Rev. Rul. 68-182, 1968-1 Cum. Bull. 263.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

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APPENDIX

Internal Revenue Code of 1954 (26 U.S.C.):

SEC. 501. EXEMPTION FROM TAX ON CORPORATIONS. CERTAIN TRUSTS, ETC.

(a) [as amended by Section 101(j)(3), Tax Reform Act of 1969, 83 Stat. 526] *Exemption From Taxation.*—An organization described in subsection (c) or (d) or section 401(a) shall be exempt from taxation under this subtitle unless such exemption is denied under section 502 or 503.

* * * * *

(c) *List of Exempt Organizations.*—The following organizations are referred to in subsection (a):

* * * * *

(6) [as amended by Section 6(a), Act of November 8, 1966, 80 Stat. 1515] Business leagues, chambers of commerce, real-estate boards, boards of trade, or professional football leagues (whether or not administering a pension fund for football players), not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

* * * * *

Treasury Regulations on Income Tax (1954 Code) (26 C.F.R.):

§ 1.501(c)(6)-1. *Business leagues, chambers of commerce, real estate boards, and boards of trade.*

A business league is an association of persons having some common business interest, the purpose of which is to promote such common interest and not to engage in a regular business of a kind ordinarily carried on for profit. It is an organization of the same general class as a chamber of commerce or board of trade. Thus, its activities should be directed to the improvement of business conditions of one or more lines of business as distingiushed from the performance of particular services for individual persons. An organization whose purpose is to engage in a regular business of a kind ordinarily carried on for profit, even though the business is conducted on a cooperative basis or produces only sufficient income to be self-sustaining, is not a business league. An association engaged in furnishing information to prospective investors, to enable them to make sound investments, is not a business league, since its activities do not further any common business interest, even though all of its income is devoted to the purpose stated. A stock or commodity exchange is not a business league, a chamber of commerce, or a board of trade within the meaning of section 501(c)(6) and is not exempt from tax. Organizations otherwise exempt from tax under this section are taxable

upon their unrelated business taxable income. See part II (section 511 and following), subchapter F, chapter 1 of the Code, and the regulations thereunder.

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